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THE SECRETARY'S  
NATIONAL CONFERENCE ON FRAUD, ABUSE, AND ERROR  
"PROTECTING THE TAXPAYER'S DOLLAR"  
U.S. DEPARTMENT OF HEALTH, EDUCATION, AND WELFARE  
WASHINGTON, D.C.

DECEMBER 13, 1978



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PREVENTING FRAUD AND ERROR AND  
INCREASING PUBLIC CONFIDENCE IN FEDERAL PROGRAMS  
TOP PRIORITIES

I welcome the opportunity to be present this morning to underscore the concern of the General Accounting Office-- and the legislative branch of the Federal Government--in the critical subject which will be addressed by this group over the next two days. While the term "Fraud, Abuse, and Error" may strike some as being somewhat negative in tone, certainly the subtitle, "Protecting the Taxpayer's Dollar," is appropriate and one to which all can subscribe without reservation. My congratulations therefore go to Secretary Califano and his associates in the Department of Health, Education, and Welfare for this constructive initiative. We will all derive much from this conference which should strengthen public confidence that the Government is actively pursuing ways to deal with these problems.

Much has been said and written in recent months--possibly too much--about the loss of confidence in Government. These statements come not only from political leaders, the investigative press, and from interest groups, but from a broad segment

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of American society. "Proposition 13" and similar actions taken by voters in many States attest to this fact. Public opinion polls support this conclusion. Summarizing these polls, a writer in the current issue of Fortune magazine concludes that "Not since the days of the Great Depression have Americans been so complaining or skeptical about the quality and character of their country's public performance." He states that Americans have lost "confidence that Government can accomplish those things the people want done \*\*." He concludes that "the tax protest is based on a genuine belief that Government can and should do all that it is doing--but much more efficiently." The call, he says, is "not for less Government but for better Government." That is what this Conference is about.

It is often stated that no one knows the extent of fraud, abuse and error in carrying out Federal programs--and that, of course, is true. But whatever the amount, it nevertheless is a matter of wide public concern just as fraud and abuse in the private sector is a concern.

I know that you will join me in the conjecture that those who abuse their public trust are a tiny fraction of the three million Federal employees who work conscientiously and honestly day in and day out; observing the highest standards of ethics in all that they do. Their reputation is

damaged--and the public confidence in Government is damaged--when a tiny minority commit fraud, where serious waste and mismanagement occur, or the Government is not able to protect itself against those who would defraud it.

Important as the detection of fraud, abuse and error is, detection should not be our primary concern as Government managers. Our prime concern should be directed toward constructing systems of management control that will prevent fraud and abuses, make it more difficult, and decrease the likelihood of error and waste. When it comes to fraud, abuse and error, the old axiom that "an ounce of prevention is worth a pound of cure" fits well.

For a moment let us examine some of the benefits of preventing rather than detecting and punishing fraud, abuses and errors. The first thing is the obvious advantage of reducing expenditures. Fraud, abuses and errors all result in the outflow of Federal dollars that Government managers are supposed to use sparingly. To the extent we prevent fraud, abuses and errors by good management systems, we stem this source of unauthorized expenditures and thus carry out our stewardship responsibilities more effectively.

However, the loss of dollars--important as that may be--is not the only cost of fraud, abuses and error. Equally important is the toll in human suffering that occurs when the perpetrators of fraud and abuse, or even sometimes errors, are discovered. While it is true that some perpetrators

of fraud and abuses are hardened criminals, a great many of them are made criminals by opportunities presented to them which they are not strong enough to resist. These opportunities usually occur because the management controls that should eliminate such opportunities have not been established; or, if established, have fallen into disuse. When such persons are caught, they suffer humiliation, loss of jobs and income, and frequently alienation from friends and family. Their lives are ruined. Often, they go to prison and that has not only a high cost in human suffering but a high cost in dollars as well. Our jails are full enough.

If we can prevent some people from committing fraud or abuses by removing temptation, we have not only served the Government but we may have saved some fellow employee from himself or herself. Even errors can cause extreme embarrassment and if serious enough, may threaten a person's employment.

#### GAO STUDY OF FRAUD POTENTIAL

With this in mind, the General Accounting Office undertook in mid-1976 an effort to ascertain whether Federal agencies had instituted effective policies and procedures for combating fraud that might exist in their programs, whether committed by Federal employees, by recipients of Federal assistance, or by others. In doing this, we had to formulate criteria regarding the composition of an effective antifraud effort. It seemed to us that the essential elements of such an effort would include

--a set of procedures to assess the vulnerability of

the programs in question. We wanted to learn if agencies had thought through the type of fraudulent schemes to which their programs were susceptible.

--the comprehensive collection and analysis of information on known incidents of fraud. The question here was whether the agencies were alert to identifying patterns or trends in the types of frauds being perpetrated.

--an aggressive effort to follow-up on instances of fraud that may have surfaced, not only to react but also actively seek out fraudulent schemes. We wanted to know whether the agencies were "policing" as well as "investigating".

--strong leadership on the part of the Department of Justice in bringing its expertise to bear on the overall problem. Our intent here was to find out if Justice was doing what it could in assisting the agencies to combat fraud.

Our next step--arduous and time-consuming--was to identify and gather evidence needed to confirm or deny the existence of the postulated problems. We reviewed activities at the Departments of Agriculture; Labor; Transportation; and Housing and Urban Development, and the Veterans Administration,

General Services Administration, and Small Business Administration. We examined these agencies' policies, procedures, and records and held discussions with their officials at headquarters and field offices of five States. We also performed work at the Department of Justice's Civil and Criminal Divisions and at various U.S. Attorneys offices. We believed this kind of coverage was necessary if we were to draw broad conclusions.

Although bright spots existed here and there with respect to an individual agency's antifraud activities, the existence of problems in the Governments' ability to fight fraud was established. Some of our findings bear repeating to illustrate the magnitude of the problem.

The Government's financial assistance programs are vulnerable targets of fraud and related white-collar crimes. Identifying the extent, nature, and frequency of these illegal acts, together with strong internal controls and effective audit coverage, are essential first steps to combating and preventing them. Yet the agencies we reviewed were not doing nearly enough to identify fraud.

Federal programs involving grants, contracts, and loan guarantees are exploited through such means as

- false claims for benefits or services,
- false statements to induce contracts or secure goods or services,

- bribery or corruption of public employees and officials,
- false payment claims for goods and services not delivered, and,
- collusion involving contractors.

#### HOW MUCH FRAUD IS THERE?

As I said, no one knows the magnitude of fraud against the Government. Hidden within apparently legitimate undertakings, it usually is unreported and/or undetected. Opportunities for fraud, however, are tremendous when you consider the magnitude of some Government disbursements. For example,

- The Veterans Administration has annual outlays of approximately \$18 billion in support of veterans benefits,
- The Department of Health, Education and Welfare has annual outlays of approximately
  - \$109 billion in Federal and trust funds in support of the Social Security system,
  - \$10.5 billion in welfare payments
  - \$10 billion in grants to States for Medicaid, and
  - \$3 billion for student assistance.
- Federal procurements in FY-1977 were almost \$80 billion, including GSA procurements for supplies and services, and DOD procurements of major

weapons systems.

We found that agencies have not established management information systems to deal with the fraud problem. They do not know the amount of identified fraud in their programs. They cannot estimate the potential amount of unknown fraud. We noted, however, that individual case data was kept which could be used as a basis to formulate such a system. Without such data, agencies have no basis for establishing the level of resources needed to combat fraud, map antifraud strategies, and evaluate the scope and effectiveness of antifraud activities.

Until recently, agencies have not made fraud detection a high priority because their overriding concern has been program execution and emphasis on such program objectives as providing loan assistance. The low priority given to fraud detection leads to passiveness regarding potentially fraudulent situations.

Also none of the agencies reviewed has, until recently designated a focal point responsible for seeking out and identifying fraud. Consequently, they generally take a reactive, rather than active, approach to fraud detection. However, a reactive approach is inadequate for detecting fraud, since there is often no specific incident to react to.

Agencies have no assurance that those personnel administering programs are referring all suspected frauds for investigation because:



- There are no controls to see that suspicious matters are reported.
- Large workloads hinder identifying suspected fraud by program personnel.
- Employees lose interest in reporting suspected frauds when follow-up actions, such as investigations and prosecutions, are not promptly taken.
- Many Federal programs are administered by State, local, or private sector institutions, and Federal agencies often unjustifiably rely on those non-Federal entities to identify and report frauds.

Agency investigators often do not have the background, experience, and training needed to effectively detect and identify fraud. About 70 percent of the staff involved in agencies we reviewed had no prior experience in fraud investigations, and about 80 percent had no formal training in investigating fraud. Where investigators have such training, it was generally limited to procurement fraud. Most investigators have also lacked the education in finance and accounting-related subjects often needed to identify fraud. Since fraud against the Government often involves examining financial documents, absence of a financial background could be detrimental to effective fraud investigations.

The Department of Justice needs to provide stronger

leadership; it has been slow to assist, coordinate, and monitor the antifraud efforts of Federal agencies.

In 1975, Justice, recognizing the need to deal with white-collar crime, established a white-collar crime committee. One activity of this committee was to provide guidance to agencies on combating fraud. It has met extensively with agency officials and has assisted agencies in carrying out several successful projects demonstrating the existence of fraud in their programs. However, the effectiveness of this "outreach" function relies on the receptivity of the agencies to Justice's encouragement and the availability of resources Justice can devote to it. From a recent conversation with the Deputy Attorney General, I am much encouraged that the Department recognizes the need for a more active role by the Department.

#### AGENCY RECOGNITION OF AGENCY ACTION

But overall, a more positive, systematic approach to identifying fraud is needed. Our report on this subject was issued in September of this year. It contains specific recommendations to assist Federal agencies in their efforts to address comprehensively the fraud and abuse problem. I am hopeful that agencies will respond by following up on reports of the General Accounting Office and internal auditors.

I am happy to report to this conference that aggressive

action has been taken:

- Before passage of legislation establishing Inspector Generals, several agencies such as Agriculture, HUD, VA, and Labor, administratively set-up an Inspector General type operation.
- The White Collar Crime Seminar sponsored by Inspector Generals from the Departments of HEW, HUD, and Agriculture.
- Among the agencies we reviewed, HUD's operational surveys are the most ambitious systematic mechanism aimed at actively seeking out and identifying fraud. The operational survey combines HUD investigators and auditors in a team which concentrates its efforts on a single HUD office. The surveys are aimed at uncovering deficiencies in program management and identifying specific irregularities, which indicate possible fraud, for investigation.

#### ESTABLISHMENT OF A GAO TASK FORCE

As a follow-up on our report, I have established a Special Task Force for the Prevention of Fraud and have allocated substantial staff resources to assist the Task Force. The major responsibility of this group will be to:

- evaluate the adequacy of the management control systems in Federal agencies that are

necessary for the prevention of fraud, and  
--assess the adequacy of the follow-up and  
corrective actions taken on reports of auditors  
and investigators.

When systems have been properly developed and are functioning as planned, the possibility for fraud, theft, or error is greatly diminished. Where the systems do not exist, or are not being used properly, the opportunities to defraud the Government and the possibilities of error increase dramatically.

I intend to have the Task Force concentrate on agency controls over cash and receivables, inventories and supplies, and anything else of value that might be stolen or misappropriated if controls are weak. Since computer systems offer many possibilities for fraud, we will identify weaknesses in computer controls over payrolls, payments to vendors, and cash disbursements for other purposes. We will also be looking at the controls in effect to ensure that the Government gets what it pays for, and that work set out in contracts is actually performed.

The Task Force will analyze the reports of internal auditors in each agency it reviews, giving particular attention to indications of fraud or error the auditors have uncovered. Where these reports or our reviews show that controls are weak, we will search for potentially

fraudulent situations, using our own computerized data retrieval and analysis packages where practicable. At the conclusion of our work at each agency, we will prepare a report to the Congress and the agency involved, with particular emphasis on any weaknesses in management controls that would permit fraud, theft, or error to occur.

Based on our findings to date, we are assigning the highest priority to fraud and abuse reviews. In fact, we will pull people off other high priority work, and as our work progresses, we may find it necessary to allocate even more staff. With the Task Force acting as the central or focal point, all our work on fraud and abuse will be brought under the umbrella of the Task Force. This procedure permits us to develop an operational capability very quickly. Task Force members are already working to coordinate fraud and abuse type reviews planned or on-going within all our divisions. By mid-January, we expect to have our first list of specific reviews.

Since prevention will merit top priority in the fight against fraud at GAO, our work will concentrate on fixing or strengthening control weaknesses found in agency systems that permit fraud to occur. One of the best ways to prevent fraud and abuse is a series of checks and balances called internal controls. For example, when these controls operate effectively, one employee's

work is usually checked by another in such a way that no one employee can abscond with agency assets without detection. The system also tends to identify error. Although no system is entirely foolproof, an effective series of checks and balances greatly decreases the likelihood that fraud and abuse will occur.

As we uncover potential fraud and abuse, we will be looking for patterns that can be explored in other agencies. And, as individual cases of potential fraud and abuse are disclosed, we plan to work closely with staff of the newly established Inspector Generals, and the Department of Justice to assist in conducting investigations necessary for prosecution. We are working out detailed procedures that will provide GAO periodic status reports on all cases referred to the Inspector General or Justice. Generally, we view our role as one of prevention rather than criminal investigation and prosecution.

#### IMPORTANCE OF AGENCY ACCOUNTING CONTROLS

As most of you know, the General Accounting Office is responsible for approving agency accounting systems. We approve the design of such systems, in many cases before they are installed. In performing our work, we give a great deal of consideration to what controls are provided for and how they will be implemented. We are frequently appalled when we return to audit such systems after they have been installed because we find that many of

the controls we considered important have been dropped.

Let me give you two simple illustrations. A "hash total", for example, is a very important control over card input to computers. This is simply a total of some number from all the cards and is used to be sure that all the cards go into processing. If a card is lost, the total will be wrong and the operator of the system will know a card is missing. Similarly if some one introduces an extra card, the total will also be wrong and the operator again alerted. In our audits we find time and time again that this simple control is not operating although the system design called for it. When we inquire as to why the procedure was dropped, we receive answers like "It took too long to check out all the cases where the totals did not agree" or "our workload increased so much we had to drop something".

A second control that we find is frequently overlooked is the "limit check." This control is usually used in payroll systems. Limit checks should reject any payment for more than the biweekly pay of a GS-18 and require special processing for any checks over that amount. This prevents the kind of error often associated with computers, that is, the issuance of a payroll check for some exorbitant amount like \$99,999.99. It also prevents anyone from running a fraudulent check through the payroll system for any amount over the biweekly pay. The limit check alone is not enough to prevent fraud,

abuses or error but coupled with other similar procedures it can be effective. It is also a simple procedure because it can be built into the computer program. Yet time after time in our audits we see that limit check has been dropped because it requires some additional effort when rejects occur.

Today the problem of financial controls is changing--radically changing--and as the direct result of the use of computers. I do not intend to demean computers. They enable us to perform many Government functions much more economically than we could perform them manually. Moreover, many functions we perform today in Government would be virtually impossible without the computer. However, computers have complicated the internal control problem and we need to change our methods to adapt to the computer.

In some of the more advanced systems we see today, the documents involved are often thousands of miles apart; a purchase order in New York, a receiving document in California and an invoice in Washington, D.C. In some cases, particularly for small purchases, the transaction may occur in its entirety without any meaningful examination of physical data by any Government employee. The order is generated by the computer when stocks get too low; the goods are received and the computer notified. The invoice is received and the computer notified; and the match of the documents is made by computer and a disbursement authorized by the computer.



Finally, the check is signed by a signature insert in the computer and no one has really examined the whole transaction. For such a system, the old ways no longer work.

We need a whole new set of controls based on the way the computer system operates. Moreover, when we rely so extensively on computers, it is essential that these new control systems be in good working order, for we have nothing to rely on to protect the Government against fraud, abuses and error except the control systems.

We had roughly 500 years after the Italians invented double entry bookkeeping to develop internal control systems for manual accounting systems and even then they were not perfect. We have only had about 20 years since computers became used extensively to adapt the internal control approach to computers. Frankly, much remains to be done to get the internal controls in such systems to a level that we can feel comfortable about them. Moreover, a system of surveillance is needed to see that the controls we have do not fall into disuse.

If these control systems are to function effectively, top management must take a direct interest in seeing that they work. Accountants and auditors are, of course, key people in this process but if these systems are to be kept in repair and a viable protection against fraud, abuse and error, management also needs to be concerned. The needed controls often require that functions be performed

outside the accountant's area of responsibility and therefore may extend beyond his purview. Due to other priorities, the auditor's work may not be done with sufficient regularity to see that controls are kept up-to-date. Management must see that all the responsible officials cooperate in setting up the necessary controls and that the personnel resources necessary to keeping them effective are devoted to the task.

Lest I be accused of not considering cost, I want to add here that all controls have to be weighed in the cost-effectiveness scale. We call this risk analysis at GAO and by it we mean assessing the potential damage the lack of a control might permit and comparing the cost of the control with that potential damage. It is possible to be overcontrolled; however, from what our audits have disclosed, I doubt that most Government agencies have too much to worry about in that regard--at least for the immediate future.

#### GROWING CONGRESSIONAL INTEREST

The Congress has recognized the need for better control in the private sector in the Foreign Corrupt Practices Act. The section of the act prohibiting corrupt payments is well known. The act also contains a less well known section requiring affected corporations to devise and maintain an adequate system of internal accounting controls sufficient to ensure that transactions are executed in accordance with management's authorizations, that transactions are properly recorded, that access to corporate assets is controlled, and that assets and

records will be compared and reconciled at reasonable intervals. Such a system is a goal all Federal agencies might well strive for.

From my nearly 40 years' experience in both the executive and legislative branch of the Federal Government, I have seen the value of audits and investigations and the changes they can bring about. Therefore, I do not downplay their significance in any way but for our purpose today, audit and investigations will be a big help, but alone, they will not be enough. Federal auditors and investigators have many priorities, they do not ordinarily perform detailed audits of procedures to see that they are working on a routine, periodic basis. Unless they, or someone else, does make such reviews, it will be hard to keep effective internal control systems going.

Unfortunately, auditing and investigative staffs have had low priority. Accounting and auditing have generally received little attention until and unless something goes wrong. This situation is changing however, with the newly enacted legislation which created Inspectors General in 14 major Departments and Agencies, reporting directly to the agency head or his deputy and given a specific statutory mandate by law. Of particular interest to us in the GAO is the provision authorizing us to set audit standards to be followed by the Inspectors General in carrying out the functions assigned to them by the Act. As many of you

know, we have had standards for Governmental audits since 1972. These standards are entitled, Standards for Audit of Governmental Organizations, Programs, Activities and Functions, but are usually called the yellow book because their formal name is so long. We will be reviewing these standards during the next year to see if they should be supplemented to give more emphasis to the need to prevent and detect against fraud, abuses and error. We welcome the suggestions which I hope and believe this conference will bring about.

#### ETHICAL STANDARDS ARE BASIC

Before concluding, I would like to say just a word to stress the importance of high ethical standards for Federal employees. Again, we should remind ourselves that fraud, abuse, and error have two origins. One is with Federal employees themselves and the other with those outside of Government who take advantage of weaknesses in the Government's financial controls to obtain personal profit for themselves. However, there are a great many cases where both elements are involved. A strong ethical awareness among Federal employees will do much to remove the temptation for these employees to violate the trust which has been vested in them and to make them more aware and sensitive to the violation of such standards by others.

President Carter has had much to say on the subject of ethics and his leadership has undoubtedly had much to do with interest on this subject in the Congress itself. And I might

add that the General Accounting Office has given very high priority to the review of financial disclosure systems, ethical standards, and, in the end, the monitorship of these standards by the executive agencies. We recommended and the Congress established an Office of Ethics to administer the Executive Branch program in the Ethics in Government Act of 1978. I believe this Act will do much to enhance employee conduct and add to the integrity of the Federal Government's operations. It is an important step in preventing temptation, conflict of interest, fraud and other abuses.

Last week, I attended a program celebrating the 100th anniversary of the establishment of the Office of Auditor General of Canada and heard a leading British Member of Parliament give a brilliant address on the importance of audit and accountability in government. He observed that democracy, like love, will withstand all attacks except indifference and neglect. He concluded that the role of the auditor serves to remind us that "if we do not learn the lessons of history we will be condemned to relive it." In this Conference, we need to remind ourselves of the public trust we hold and to act--and to act visibly--to do whatever we can to demonstrate to the entire Nation that we can act responsively and responsibly in protecting the taxpayer's dollar.